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Agenda Item 7a

June 14, 2011

TO: MEMBERS OF THE BENEFITS AND PROGRAM ADMINISTRATION COMMITTEE

I. SUBJECT: Public Employee Compensation Update

II. PROGRAM: Customer Account Services Division

III. RECOMMENDATION: Information Only

IV. ANALYSIS:

The purpose of this agenda item is to provide a summary update on efforts made by CalPERS staff and other interested parties based upon recommendations from members of the Board of Administration and the CalPERS senior and executive management team over the past nine calendar months.

The City of Bell spotlighted the risk concerning illegal inflation of compensation, leading to enhanced retirement allowances. In consideration of our fiduciary and ethical responsibilities, CalPERS immediately undertook the following actions to address the issue:

- CalPERS adopted California Code of Regulation (CCR) 570.5, Publicly Available Pay Schedule and Written Labor Policy or Agreement, and amended CCR 571 at the Board of Administration meeting on April 12, 2011. The purpose of the regulations is to enhance disclosure and transparency of public employee compensation.

- CalPERS staff completed a review of fifteen members with reported compensation in excess of $400,000. The compensation of twelve of the members was determined to be compliant with statutes and regulations. Of the three members not in compliance:

    - One member was the Chief Administrative Officer with the City of Bell. Compensation was limited to that of the last publicly available pay schedule;
    - It was determined that one member did not qualify for membership;
    - One member was denied an item of special compensation.

- CalPERS staff implemented escalation procedures and guidelines to identify to CalPERS management unusually high compensation and payrate increases reported by employers. This ensures reported compensation has been approved at the appropriate management level.

- CalPERS staff completed a sample review of members with reported compensation exceeding the Internal Revenue Code 401(a)(17) limit of $245,000. Based on this review it was determined that the reported compensation for 44 of the 45 members was in compliance with current statutes and regulations. The one member denied was due to a payrate issue.

- CalPERS staff provided technical assistance to the Public Employee Compensation and Benefit Task Force (Compensation Subgroup) and stakeholders. In addition, CalPERS staff assisted the Office of the Attorney General with its investigation surrounding the salaries and other compensation of public employees. CalPERS provided pension expertise on various legislation proposals aimed at improving disclosure and transparency.

- The State Controller created a new website that lists the salary, pension benefits and other compensation for California's city and county employees to increase transparency.

- CalPERS staff conducted several high profile public agency reviews including, but not limited to, the Cities of Bell, Vernon, Maywood and Industry. Beginning fiscal year 2010-2011 the Office of Audit Services (OFAS) posted all reviews online. This provides the general public and stakeholders with information on public agency compliance with CalPERS' statutes and regulations. OFAS now highlights significant findings in the quarterly status report to the Finance Committee.

- CalPERS staff collected and recorded various aspects of 2,250 compensation determinations performed between September 1, 2010 and February 28, 2011 to identify common issues and trends. The data analysis included items such as: the number of determinations that required adjustments, the number of denials, and the number of determinations that had no compensation issues. We also gathered information on group or class size, employer type and member classification.

  Of the 2,250 determinations, we found that 329 required adjustments to the compensation used in the retirement allowances. Reporting errors accounted for 317 of the 329 adjustments. The remaining 12 determinations resulted in denials of compensation. Nine denials were related to the amount of special compensation reported and three denials were for payrates not compliant with the salary schedule or employment contract. None of the denials were due to limiting the compensation based upon the average salary increase of the group or class.

During our analysis we found 204 members who belonged in a group or class of 15 or less. Their average salary increase during their final compensation period was 4.38%. Compensation was denied for eight members; five for special compensation and three for payrates not in compliance with statute or regulations. We did not see unique problems with the compensation of these employees, but rather the denials represented the same issues found throughout the entire population.

Reviews escalated for special compensation issues accounted for over 85% of all reviews, and of those, almost 15% required some type of reporting adjustment by the employers. With the new my|CalPERS system we will have the ability to determine if special compensation is in compliance when payroll is entered into the system by the employer. The analysis shows that there also needs to be more training for employers on how to accurately report special compensation.

Across all other demographics, we discovered that most denials pertained to members who had the ability to control or influence their own compensation. CalPERS will begin focusing more resources on reviewing those member who earn the highest compensation at each agency. Although the amount of compensation paid to the member is determined by the agency, CalPERS staff will work with the agency to ensure that the reported compensation is in compliance with all statutes and regulations.

We will use the results of our determinations to improve our procedures and refine our edits and parameters in conjunction with the new my|CalPERS system. We will also provide enhanced education to our employers on proper reporting of compensation.

In summary, we have taken significant actions to address concerns raised by recent salary controversies. We put in place mitigation techniques to ensure inflated compensation would be captured and addressed. We studied our policies and procedures for ways to improve our ability to pinpoint and correct this type of abuse. This resulted in changes to our edits and parameters to detect offenders, increasing the focus on compensation during employer reviews and increased management review of all determinations.

We found that we needed to partner more with members of the public in our vigilance to stop pension spiking. We published employer reviews on the internet and adopted regulations making it easier for members of the public to obtain the information necessary to monitor the compensation of public agency members.

Staff practice had been to focus on reviewing a member's account at the time of retirement. With the my|CalPERS system, staff will have the ability to review the reporting of compensation for all employers on a global basis. This will allow an in-depth analysis of Memorandums of Understanding, salary schedules, employment contracts and other related documents to ensure the agencies are reporting their payrate and special compensation items correctly. In addition, we will leverage the new system to obtain reports based on high wage earners who are nearing retirement, and will review their compensation as well. This will improve customer service, reduce overpayments and provide a more thorough and accurate approach to compensation review.

We found that CalPERS agencies are predominantly in compliance with reporting requirements. We are confident that the improvements we are making to our processes coupled with a heightened awareness of where to focus our resources, will help us detect and correct the small minority of pension abuse cases, and the incorrect reporting of compensation.

V. STRATEGIC PLAN:

This item is not a specific product of the Strategic or Annual Plans, but is part of the regular and ongoing workload of the Customer Account Services Division and other affected divisions.

VI. RESULTS/COSTS:

None

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